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SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1955.

No. 953

WILLIAM M. LIDDON and MARIA PROTHRO LIDDON,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR A WRIT OF CERTIORARI

To the United States Court of Appeals for the Sixth Circuit.

JOHN J. HOOKER,
K. HARLAN DODSON, JR.,
1106 Nashville Trust Building,
Nashville 3, Tennessee,
Attorneys for Petitioners.

ST. LOUIS LAW PRINTING CO., 415 North Eighth Street. CEntral 1-4477.

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To the United States Court of Appeals for the Sixth Circuit.

To the Honorable Chief Justice and the Associate Justices of the Supreme Court of the United States:

Petitioners, William M. Liddon and Maria Prothro Liddon, pray that a writ of certiorari issue to review an order and judgment entered by the Court of Appeals for the Sixth Circuit on February 11, 1956, and an order denying a petition to rehear dated March 9, 1956, which said order and judgment affirmed in part the action of the Tax Court of the United States wherein the Tax Court sustained the finding of the Commissioner of Internal Revenue that the

dissolution and liquidation of Liddon Motors, Inc., in 1938 was a reorganization so that petitioners were not entitled to treat their liquidating dividend as capital gain.

OPINIONS BELOW.

The opinion of The Tax Court of the United States is reported in 22 T. C., at page 1220, and a copy of the same may be found as an appendix to this petition. The opinion of the United States Court of Appeals for the Sixth Circuit has not yet been reported but may be found as an appendix to this petition.

JURISDICTION.

The judgment of the United States Court of Appeals for the Sixth Circuit overruling the petition to rehear was entered on March 9, 1956, and the jurisdiction of this Court is invoked under the provisions of Title 28, Section 1254 (1) of the United States Code.

QUESTION PRESENTED.

The question presented for review by this petition is whether the gain resulting from the liquidation of a corporation, Liddon Motors, Inc., which was dissolved and liquidated in 1948, is taxable as ordinary income under Section 112 (c) (2) Internal Revenue Code of 1939 or as a capital gain under Section 115 (c) of the Internal Revenue Code of 1939.*

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* It was the insistence of the Commissioner of Internal Revenue in The Tax Court that if in fact there was not a reorganization within the meaning of Section 112 (c) (2), Internal Revenue Code, then Section 115 (g) of the Internal Revenue Code applied on the premise that there was a stock redemption equivalent to the distribution of a taxable dividend. This insistence of the Commissioner was not considered by The Tax Court or the Court of Appeals for the Sixth Circuit.

STATUTES INVOLVED.

The determinative statutes are certain portions of the Internal Revenue Code of 1939, these being Section 112 (c) (2) and Section 115 (c). Section 112 (c) (2) of the Internal Revenue Code of 1939 provides as follows:

"(c) **Gain from exchange not solely in kind.**

. . . . . .

"(2) If a distribution made in pursuance of a plan of reorganization is within the provisions of paragraph (1) of this subsection but has the effect of the distribution of a taxable dividend, then there shall be taxed as a dividend to each distributee such an amount of the gain recognized under paragraph (1) as is not in excess of his ratable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913. The remainder, if any, of the gain recognized under paragraph (1) shall be taxed as a gain from the exchange of property."

Section 115 (c) of the Internal Revenue Code provides in part as follows:

"115. **Distributions by corporations.**

. . . . . .

"(c) **Distributions in liquidation.** Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. In

the case of amounts distributed (whether before January 1, 1939, or on or after such date) in partial liquidation (other than a distribution to which the provisions of subsection (h) of this section are applicable) the part of such distribution which is properly chargeable to capital account shall not be considered a distribution of earnings or profits . . ."

STATEMENT OF THE CASE.

The petitioner William M. Liddon entered into the field of Pontiac automobiles sale and distribution in the Nashville, Tennessee, area in January of 1936, operating first as a corporation and then as a partnership, the partners being the petitioner William M. Liddon, his wife, the petitioner, Maria Prothro Liddon, and R. H. Davis (Appellants' Appendix Below, p. 46a). From April, 1942, to April, 1946, petitioner William M. Liddon was in the Army on active duty, and R. H. Davis served as the manager of the business. (Appellants' Appendix Below, p. 46a). Upon his return from the service petitioner William M. Liddon actively re-engaged in the business, and on August 1, 1946, two Tennessee corporations were formed to take over the business of the partnership, one of these being formed to take over the sale and distribution of Pontiacs, and the other was formed to take over the sale and distribution of White Trucks (Appellants' Appendix Below, p. 75a). The Pontiac corporation, known as Liddon Motors, Inc., remained in existence until July 17, 1948, when its charter was finally surrendered (Appellants' Appendix Below, p. 47a, Petitioner's Exhibit No. 1), pursuant to the authorization of the Board of Directors and Stockholders in a meeting on April 26, 1948 (Appellants' Appendix Below, p. 56a). Liddon Motors, Inc., had an authorized capital stock of 10,000 shares, $10.00 par value (Appellants' Appendix Below, p. 48a); of which 680 shares were issued to

William M. Liddon, 680 shares to Maria Prothro Liddon and 340 shares to R. H. Davis (Appellants' Appendix Below, p. 49a).

In April of 1948, R. H. Davis had a heart attack, and thereupon tendered his resignation as General Manager of Liddon Motors, Inc., on April 26, 1948, by letters addressed to both Liddon Motors, Inc. (Appellants' Appendix Below, pp. 50a, 100a), and Pontiac Division of General Motors (Appellants' Appendix Below, pp. 50a, 51a). Upon receipt of such notice, Pontiac Division of General Motors immediately cancelled the franchise pursuant to Section 3 of the Contract (Appellants' Appendix Below, p. 121a, Petitioner's Ex. 5). At that time Davis offered his stock in the corporation but a price could not be agreed upon, and the offer for retirement so that he might go to Texas immediately, pursuant to his doctor's insistence, rather than await the complete liquidation, was refused (Appellants' Appendix Below, p. 76a). Liquidation was commenced, and by June 4, 1948, the liquidation was sufficiently far along that it became apparent that R. H. Davis's share of the assets upon liquidation would be equivalent to $11.00 per share for his stock, and his health had become so poor that his doctor was by then even more insistent that he leave Nashville immediately, and to accommodate him, the liquidating corporation, Liddon Motors, Inc., purchased and retired his stock for $11.00 per share, which was almost exactly the value it would have had upon final liquidation (Appellants' Appendix Below, pp. 57a, 65a, 76a, 100a, Petitioner's Exhibits 16 and 18).

The franchise agreement which Liddon Motors, Inc., and all other Pontiac dealers and distributors had with the Pontiac Division is in the main a form contract, but the important section is not, this being the part which is renewed each year and which designates the individuals upon whose association with the agency the continuance of the contract

depends (Appellants' Appendix Below, pp. 51a-52a). The language of this section of the agency contract which was in effect on April 26, 1948, was:

> "Third, this agreement constitutes a personal contract having been entered into in reliance upon and recognition of W. M. Liddon, R. H. Davis, jointly, the dealer or partners in the dealership or representatives of the dealer who actively and substantially participate in the ownership and/or operation of the dealership, dealer shall not transfer nor assign this agreement or any part thereof nor make nor suffer to be made any substantial change in the ownership, financial interest, or active management of dealer" (Appellants' Appendix Below, p. 53a).

This made the contract a personal contract or franchise, and while Liddon Motor was the designated name of the dealer, it was not a contracting party, the agreement being between Pontiac Motor Division of General Motors on the one hand and William M. Liddon and R. H. Davis on the other.

In the event of any change in such persons designated in this section of the contract, General Motors cancels the contract (Appellants' Appendix Below, pp. 54a, 82a, 102a), and based upon the resignation of R. H. Davis canceled the agency contract in its entirety (Appellants' Appendix Below, pp. 51a, 81a-82a, 93a, 101a). The termination section of the contract in effect on April 26, 1948, was:

> "Seller may terminate this agreement immediately by delivering to dealer or his representative written notice of such termination in the event of the happening of any of the following:
>
> "(a) Death, incapacity or the removal, elimination or resignation from the dealership for any reason of

the dealer or any person named in paragraph third of this agreement'' (Appellants' Appendix Below, pp. 54a-55a, Petitioner's Exhibit 5).

On May 1, 1948, approximately 2½ months before Liddon Motors, Inc., was dissolved, a Tennessee corporation, Liddon Pontiac, Inc., was formed, in which William M. Liddon owned 1,250 shares, Maria Prothro Liddon owned 1,250 shares and Oscar Sanders 1 share (Appellants' Appendix Below, pp. 56a, 59a, 96a). This corporation was formed with the personal funds of William M. Liddon in the amount of $3,000.00, with the personal funds of Maria Prothro Liddon in the amount of $2,000.00 and of Oscar Sanders in the amount of $10.00 (Appellants' Appendix Below, pp. 61a-62a). Some 2½ months before Liddon Motors, Inc., was liquidated or any funds received by either William M. Liddon or Maria Prothro Liddon out of the liquidation of Liddon Motors, Inc. (Appellants' Appendix Below, p. 62a), Liddon Pontiac, Inc., was chartered and commenced business. Subsequently, and on May 21, 1948, William M. Liddon and Maria Prothro Liddon put an additional $20,000.00 of their money into Liddon Pontiac, Inc.; this likewise before anything was received by them, or either of them, from the liquidation of Liddon Motors, Inc. (Appellants' Appendix Below, pp. 63a-64a). Subsequently, and on December 31, 1948, an additional 3,513 shares of the stock of Liddon Pontiac, Inc., were issued to William M. Liddon and Maria Prothro Liddon each, and 100 shares issued to Oscar Sanders (Appellants' Appendix Below, p. 96a). In other words, none of the operating capital of Liddon Pontiac, Inc., for the entire year 1948 came out of Liddon Motors, Inc., either before or after liquidation, directly or indirectly (Appellants' Appendix Below, p. 70a).

Liddon Pontiac, Inc., obtained a Pontiac franchise on May 1, 1948 (Appellants' Appendix Below, pp. 59a-60a,

82a), with William M. Liddon as the designated individual in the contract, this because William M. Liddon met the requirements of General Motors as such designated individual (Appellants' Appendix Below, pp. 85a, 92a-93a). On May 6, 1948, Liddon Motors, Inc., was authorized to negotiate with Liddon Pontiac, Inc., with respect to the sale of **some** of the assets of Liddon Motors, Inc., which could be best used only by a Pontiac distributor, Liddon Pontiac being the only logical purchaser for such assets (Appellants' Appendix Below, pp. 56a, 67a), and on June 4, 1948, Liddon Pontiac, Inc., purchased some of these assets (Appellants' Appendix Below, pp. 66a-68a, Petitioner's Exhibit 15). There was no transfer of assets within the meaning of Section 112 (g) (1) (D), but an outright sale of a small portion of the assets of Liddon Motors, Inc., peculiar to the business of selling Pontiacs, to the only logical purchaser. The other assets of Liddon Motors, Inc., were gradually liquidated out and the liabilities paid at a time when Liddon Pontiac, Inc., was in full operation (Appellants' Appendix Below, p. 68a).

As pointed out above, Liddon Motors, Inc., had never paid any dividends, and this was for the reason that General Motors required a large dealership capital based upon many factors, i. e., dealership required working capital and Liddon Motors, Inc., was trying to build up to this required amount so as to retain its franchise (Appellants' Appendix Below, pp. 62a, 77a, 78a, 87a, 91a, 97a-99a). When prior tax returns were filed and examined, no question was ever raised that there was an improper accumulation of surplus.

There was no requirement that any of the stockholders of Liddon Motors, Inc., go into or invest any capital in Liddon Pontiac, Inc., and only two of the three stockholders of Liddon Motors, Inc., did so (Appellants' Appendix Below, pp. 69a, 101a); and there was never any considera-

tion given or discussion of a merger or a reorganization of Liddon Motors, Inc. (Appellants' Appendix Below, p. 71a).

The Court of Appeals for the Sixth Circuit in a dividend opinion affirmed the Tax Court and refused to apply the rule announced by that Court in the case of **United States v. Arcade Company**, 203 F. (2d) 230, for the reason that in the **Arcade Company** case the assets were distributed to trustees before being transferred to the newly formed corporation in return for its stock; whereas, in the instant case no such subterfuge was used. The opinion of the Court in the **Arcade Company** case was written by McAllister, Circuit Judge, who dissented in the instant case.

REASONS FOR GRANTING THE WRIT.

1. The opinion of the United States Court of Appeals for the Sixth Circuit in the case at bar is in conflict with the opinion of that Court in the case of **United States v. Arcade Company**, 203 F. (2d) 230, on an important question of Federal Tax law, which has not been, but should be, settled by this Court.

Under the existing statutes taxpayers when liquidating a corporation must gamble on the question of what judges will constitute the Court of Appeals for the Sixth Circuit in the event such liquidation is questioned by the Commissioner. If the Court is constituted of those judges or a majority of the Court is constituted of those judges who decided the **Arcade Company** case for the Court, then the liquidation and resulting capital gain treatment will be sustained; whereas, if the majority of the Court is constituted of those judges hearing the case at bar, a reorganization will be found with the result that liquidating dividends will be treated as ordinary income.

This question is not a question so remote as to arise infrequently because as the record in this case shows automobile agency contracts are generally of the same type as the agency contract here involved, and in the event of the death or disability of one of the contracting parties to whom the manufacturer looks in the contract, the contract automatically terminates and the probabilities of the need for a dissolution arise.

The only distinction between the case at bar and the **Arcade Company** case [and the only distinction between this case and the case of **Braicks v. Henricksen** (D. C., Washington), 43 F. Supp. 254], is that in those cases all of the assets were distributed to trustees for the stockholders and then exchanged by the trustees for stock in the newly formed corporation; whereas, in the instant case no subterfuge was used, and, on the contrary, there was a bona fide sale for cash of a small part of the assets of the old corporation. The proceeds from the sale of these few assets were distributed along with all of the other assets of the old corporation to its stockholders in complete liquidation and **no part** of these assets received in liquidation went into the new corporation. This distinction is one of form and not of substance.

The only reason these assets were sold to the new corporation rather than to someone else was because the new corporation was the only market in which such particular assets could be sold for their reasonable value.

As was pointed out in the dissenting opinion, which opinion was prepared by the author of the opinion in the **Arcade Company** case, the old corporation because of the retirement of its general manager had lost its most important business assets, its franchise dealer contract. There was nothing false, suspicious or contrived about this situation. When a sale could not be agreed upon for the stock

of Mr. Davis, who was retiring, there was no alternative except to liquidate the old corporation, and when the new corporation, which has been termed a reorganization in the Court below, was formed with new capital having no connection or relationship with the old corporation, none of the assets of the old corporation had been received by the new one or by the petitioners through sale, transfer, or otherwise. The new company was formed with new money added, a new dealer's franchise contract and any assets which it received from the old corporation it bought at an outright sale for cash. The most important asset of the old corporation, the dealer franchise contract, could not have been transferred to the new corporation.

The Court of Appeals for the Sixth Circuit, with judges other than those constituting a majority of the Court in the instant case, found, in both the case of **Mascot Stove Company v. Commissioner**, 120 F. (2d) 153, and **Glenn v. Courier-Journal Job Printing Company**, 127 F. (2d) 820, in which latter case the Court was dealing with a case involving Section 112 (g) of the Internal Revenue Code, that is, the reorganization provision, that "Liquidation is the Antithesis of Reorganization." Yet in the case at bar that same Court found on this most important question of tax law that there was a liquidation, but there was also a reorganization.

Again, this leaves the taxpayer in the unfortunate position of having to speculate as to which rule will be applied when his case finally reaches the Court of Appeals for the Sixth Circuit.

CONCLUSION.

For the reasons stated, we respectfully submit that the petition for the writ of certiorari should be granted in the instant consolidated cases and the decision of the

Court of Appeals reversed in order that taxpayers and their advisors might be in the position to determine with some degree of accuracy the taxable effect of a corporate liquidation when there is no alternative except to liquidate.

Respectfully submitted,

JOHN J. HOOKER,
K. HARLAN DODSON, JR.,
1106 Nashville Trust Building,
Nashville 3, Tennessee,
Attorneys for Petitioners.

APPENDIX A.

DECISION.

22 T. C. No. 150.

The Tax Court of the United States.

William M. Liddon, Petitioner, v. Commissioner of Internal Revenue, Respondent.

Maria Protho Liddon, Petitioner, v. Commissioner of Internal Revenue, Respondent.

Docket Nos. 41495, 41497. Filed September 21, 1954.

Reorganization—Distribution in Liquidation—Section 112 (c) (2)—Section 115 (c).—An old corporation in liquidation sold some of its assets to a new corporation. At the time petitioners held more than 80 per cent of the stock in both corporations. Shortly thereafter petitioners acquired the remaining assets of the old corporation in exchange for their stock. **Held,** that the liquidation of the old corporation was under a plan of reorganization, and the gain resulting from the liquidation of the old corporation was taxable to petitioners under section 112 (c) (2).

John J. Hooker, Esq., and Albert B. Maloney, C. P. A., for the petitioners.

Homer F. Benson, Esq., for the respondent.

Respondent determined the following deficiencies in income tax for 1948:

Docket No.	Petitioner	Deficiency
41495	William M. Liddon	$26,598.77
41497	Maria Prothro Liddon	22,058.15

The issue is whether the gain resulting from the liquidation of a closely held corporation is taxable as ordinary income, section 112 (c) (2), or as capital gain, section 115 (c), section 111, section 112, and section 117.

Findings of Fact.

William M. Liddon and Maria Prothro Liddon, husband and wife in 1948, were residents of Nashville, Tennessee. They filed their separate tax returns for 1948 with the collector of internal revenue for the district of Tennessee. William M. Liddon will be hereinafter referred to as the petitioner.

Petitioner had been in the automobile business as a distributor of automobiles in Nashville from 1936 to the time of the hearing. During some of these years his business was operated as a closely held corporation, while in other years as a partnership. Prior to August 1, 1946, the business was a partnership composed of petitioner, his wife and R. H. Davis. On August 1, 1946, certain assets of the partnership were transferred to a corporation known as Liddon Motors, Inc., hereinafter referred to as the old corporation.

The old corporation, with an authorized capital stock of 10,000 shares with a par value of $10 per share, was organized under the laws of Tennessee to carry on an automobile business. As a result of the initial stock distribution petitioner held 680 shares, his wife 680 shares, and Davis 340 shares. Later there were stock dividends so that on April 26, 1948, petitioner held 4,000 shares, his wife 4,000 shares, and Davis 2,000 shares.

Davis was the general manager of the old corporation. However, some time in April, 1948, because of ill health, he tendered his resignation as general manager. He also notified the stockholders and directors that he had de-

cided to sell or liquidate his interest in the corporation as soon as possible.

The minutes of a special meeting of the stockholders on April 26, 1948, stated that Davis offered to sell his stock to the other stockholders, that is, petitioner and his wife, but they did not accept. The minutes related that after further discussion the stockholders decided to liquidate the old corporation and surrender the corporate charter. At this meeting Oscar Sanders was elected to the board to fill the vacancy caused by Davis' resignation.

The old corporation had an agreement with the Pontiac Motor Division of the General Motors Corporation, hereinafter referred to as Pontiac. In general this agreement was a form contract between Pontiac and one of its dealers, and the dealer might be an individual, a partnership, or a corporation. However, one of the paragraphs in the contract, designated paragraph "THIRD," contained a blank space so that individual names could be inserted. This paragraph attempted to make the agreement a personal contract even though a corporation or a partnership was denominated elsewhere in the contract as the dealer authorized to buy and resell cars. For the agreement in effect on April 26, 1948, Liddon Motors, Inc., was named the dealer. Paragraph "Third" without the inserts was as follows:

> Third: This Agreement constitutes a personal contract, having been entered into in reliance upon and recognition of ..... (jointly), the Dealer, or partner(s) in the dealership, or representative(s) of the Dealer who actively and substantially participate(s) in the ownership and/or operation of the dealership. Dealer shall not transfer nor assign this Agreement or any part thereof, nor make nor suffer to be made any substantial change in the ownership, financial interests or active management of Dealer.

Another part of this agreement also provided that Pontiac could terminate the agreement upon "Death, incapacity, or the removal, resignation, withdrawal, or elimination from the dealership for any reason of Dealer or any person named in Paragraph Third of this Agreement." In the agreement between the old corporation and Pontiac the names of petitioner and Davis were entered on the Third paragraph.

On May 1, 1948, a certificate of incorporation for Liddon Pontiac, Inc., hereinafter referred to as the new corporation was filed with the Secretary of State of Tennessee. This new corporation was authorized to issue 30,000 shares of common stock with a par value of $10. The initial capital contributions were $3,000 for 300 shares by petitioner, $2,000 for 200 shares by his wife, and $10 for one share by Sanders. The new corporation was authorized to do a general merchandising business. On the same date the new corporation entered into an agreement with Pontiac to buy and resell its automobiles. Only petitioner's name was entered in paragraph "Third" of the new agreement. Except for this change in paragraph "Third," the agreement between Pontiac and the old corporation was essentially the same as the agreement between Pontiac and the new corporation.

On May 6, 1948, at a special meeting of the board of directors the old corporation was directed to sell some of its assets to the new corporation at book value. The minutes of the meeting contain the following statement:

> * * * it was the consensus of opinion of the Board of Directors that in view of the fact that Liddon Pontiac, Inc., was the only logical prospective purchaser of the remaining assets of this Corporation, and that would entail untold expenses and many months of processing the liquidation to attempt to sell these other assets out individually, and under the terms of

the franchise, Liddon Pontiac, Inc., has a right to purchase these, that it was agreeable for Liddon Pontiac, Inc., to utilize the use of these other assets without charge during the period of inventory, negotiation, etc.

Priar to May 21, 1948, petitioner and his wife invested an additional $20,000 in the capital stock of the new corporation.

On June 4, 1948, it was explained to the board of directors of the old corporation that Davis would accept $11 per share from the corporation for his 2,000 shares. The board voted to call Davis' stock and pay him $11 per share. Davis was given a check dated June 4, 1948, for $22,000. This was paid by the drawee bank on June 5, 1948.

Among the assets of the old corporation, on or about July 13, 1948, was a $60,000 note receivable. At a special meeting of the stockholders and directors on July 13, 1948, the following was authorized:

> W. M. Liddon and Marie P. Liddon, being holders of all the outstanding stock at this time in equal shares, agreed to accept from Liddon White Truck Co., Inc., two notes of $30,000.00 each payable to W. M. Liddon and Marie P. Liddon as partial settlement of Liddon Motors, Inc., as liquidating dividend to be payable to them.
>
> In addition to this, the President was authorized to issue the Shareholders final liquidating dividend of the corporation which represented $90,000.00, in addition to the above note, to liquidate the entire outstanding stock.

The money and property petitioner and his wife each received in final liquidation of the old corporation was $75,618.64 for 4,000 shares of stock, or approximately $18.90 a share.

On July 17, 1948, an instrument entitled "State of Tennessee Surrender of Charter of Incorporation," was filed with the Secretary of State. By virtue of this instrument the corporate charter of the old corporation was surrendered and the corporation dissolved.

The old corporation filed a corporation income tax return for the period from January 1, 1948, to September 30, 1948. A summary of the balance sheets for the beginning and end of the period is as follows:

	January 1, 1948	Sept. 30, 1948
Cash	$ 66,431.76	$ 18,498.41
Notes receivable	88,719.87	100,000.00
Inventory	29,859.68	.....
Depreciable assets	13,762.21	.....
Other	11,512.92	.....
Total	$210,286.44	$118,498.41
Accounts payable	$ 15,750.77	.....
Other liabilities	61,735.15	$ 57,162.42
Capital stock	34,000.00	.....
Earned surplus	98,800.52	61,335.99
Total	$210,286.44	$118,498.41

On their 1948 tax returns petitioner and his wife each reported $75,618.64 less $6,800 as a long-term capital gain from Liddon Motors, Inc.

The respondent in the statement explained the adjustment in petitioner's deficiency notice as follows:

> (a) In your return you reported as capital gain, income received from the liquidation of Liddon Motors, Inc., $68,818.64, taxable at 50%, or $34,409.32. It is held that income so received is ordinary income, taxable at 100%, and accordingly, net income is increased in the amount of $34,409.32.

The liquidation of the old corporation was pursuant to a plan of reorganization, and the distribution of its assets in exchange for its stock had the effect of the distribution of a taxable dividend.

Opinion.

Johnson, Judge: An epitomization of the facts will aid us in discussing this case. The old closely held corporation was organized in 1946; it engaged in a successful automobile business for two years. Prior to July 17, 1948, the date of the surrender of the old corporate charter, the stock of the old corporation had been liquidated and some of its assets sold to a new corporation. This new corporation had been incorporated on May 1, 1948. The old corporation held a franchise to sell Pontiac automobiles, but this franchise was terminated prior to the liquidation of the old corporation. Another Pontiac franchise was issued to the new corporation on May 1, 1948. Petitioner and his wife held 80 per cent of the stock in the old corporation and more than 80 per cent of the stock in the new corporation. They each received a gain of $68,818.64 from the liquidation of the old corporation in 1948. In the beginning of this series of transactions petitioner and his wife held stock in the old corporation; at the termination they held stock in the new corporation plus "money-to-boot"

Petitioner contends that there was a complete liquidation of the old corporation under section 115 (c), and the gain therefrom was capital gain. In opposition respondent urges that the transactions, in substance as distinguished from form, constitute a reorganization within the meaning of section 112 (b) (4) or (5) and 112 (g) (1) (D), with the result that the gain was taxable under section 112 (c). In the alternative respondent maintains that the redemption or cancellation of the stock of the old corporation was essentially equivalent to the distribution

of accumulated earnings and profits and was a taxable dividend under section 115 (g).

We shall consider the first item of dispute between the parties, that is, whether there is a taxable gain to petitioner under the provisions of section 112 (c). The pertinent provisions of this section are as follows:

Sec. 112. Recognition of Gain or Loss.

* * * * * * *

(c) Gain from Exchanges Not Solely in Kind.—

(1) If an exchange would be within the provisions of subsection (b) (1), (2), (3), or (5), * * * of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph * * * to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property.

(2) If a distribution made in pursuance of a plan of reorganization is within the provisions of paragraph (1) of this subsection but has the effect of the distribution of a taxable dividend, then there shall be taxed as a dividend to each distributee such an amount of the gain recognized under paragraph (1) as is not in excess of his ratable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913. The remainder, if any, of the gain recognized under paragraph (1) shall be taxed as a gain from the exchange of property.

The first question to be considered is whether there was a "plan of reorganization." The Code does not define a plan of reorganization but it does define the term "reorganization" in section 112 (g) (1). There, under (D),

a reorganization means "a transfer by a corporation of all or part of its assets to another corporation if immediately after the transfer the transferor or its shareholders or both are in control of the corporation to which the assets are transferred." Control, under section 112 (h), means ownership of stock possessing at least 80 per cent of the total voting power. It is immediately apparent that the transfer of some assets of the old corporation to the new, while petitioner and his wife controlled at least 80 per cent of the voting stock of both corporations, is a reorganization as defined by the Code.

In our opinion the transfer of these assets was only one step in a series of transactions under a single plan. Even though there was no formal written plan, the various transactions—the sale of Davis' stock, the formation of a new corporation, the transfer of assets from the old to the new corporation, the liquidation of the old corporation after the new corporation was in business—all indicate a master plan of reorganization rather than the mere liquidation of the old corporation. When we must determine whether there has been a reorganization, a liquidation, a sale or an exchange in a series of transactions, it is proper for us to look at the beginning and end of the series. See **Illinois Water Service Co.**, 2 T. C. 1200, 1231. See also **William H. Redfield**, 34 B. T. A. 967, and **Richard H. Survaunt**, 5 T. C. 665, affd. 162 F. 2d 753. Cf. **Standard Realization Co.**, 10 T. C. 708; **Charles R. Mathis, Jr.**, 19 T. C. 1123. It is also proper for us to consider all of the transactions together rather than separately. **Helvering v. Alabama Asphaltic Limestone Co.**, 315 U. S. 179. And if in fact there was a "reorganization" of the old corporation, the liquidation was merely one of the steps in the integrated transactions. **W. N. Fry**, 5 T. C. 1058, 1067.

Now that we have determined that there was a plan of reorganization and a distribution to petitioner and his

wife pursuant to that plan, we must determine if the distribution was within the provisions of paragraph (1) of section 112 (c). Paragraph (1) refers to section 112 (b) (3) which deals with exchanges solely in kind when stock is exchanged for stock. That section is as follows:

> (b) Exchanges Solely in Kind.—
>
> * * * * * * *
>
> (3) Stock for Stock on Reorganization.—No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

When section 112 (b) (3) is read under the provisions of section 112 (c) (1) there must be an exchange of stock for stock plus something "to boot."

Returning to the facts again, during the liquidation of the old corporation petitioner exchanged his stock for money. In form this was not an exchange of stock for stuck plus something "to boot." However, all of the transactions, when viewed as one plan of reorganization, culminated in an exchange of stock for stock plus money. Under section 112 (c) (1) the gain in the amount of money that petitioner received should be recognized.

If this gain is recognized should it be taxed? Section 112 (c) (2) answers "yes" if the distribution "has the effect of the distribution of a taxable dividend." It should be pointed out that for this section of the Code there is no difference between liquidating dividends and ordinary dividends. **John S. Woodard**, 30 B. T. A. 1216, 1227. Cf. section 115 (c).

An examination of the legislative history of section 112 (c) (2) will aid us in determining the legislative in-

tent of this section. In **John S. Woodard,** supra, we established that section 112 (c) (2) first appeared in the Revenue Act of 1928 as section 203 (d) (2) of the 1924 Act. From an analysis of the House Ways and Means Committee and the Senate Finance Committee reports on the Revenue Bill of 1924[1], we pointed out that the primary purpose of Congress in enacting section 203 (d) (2) was to prevent the taxing of liquidating dividends, to the extent of accumulated earnings, at the capital gain rate. It is significant that the wording of section 112 (c) (2) as found in the 1928 Act has been unchanged through the years.

We recognize that the money petitioner received was not in fact dividends, but we also believe that to the extent of the accumulated earnings, the liquidation of the stock had the effect of the distribution of taxable dividends. The record fully supports this conclusion. There was no evidence that the old corporation paid any dividends other

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[1] (2) There is no provision of the existing law which corresponds to paragraph (2) of subdivision (d). This subdivision provides that any amount distributed by a corporation in connection with a reorganization which has the effect of a taxable dividend shall be taxed as a dividend and not as a taxable gain.

The necessity for this provision may best be shown by an example: Corporation A has capital stock of $100,000, and earnings and profits accumulated since March 1, 1913, of $50,000. If it distributes the $50,000 as a dividend to its stockholders, the amount distributed will be taxed at the full surtax rates.

On the other hand, corporation A may organize Corporation B, to which it transfers all its assets, the consideration for the transfer being the issuance by B of all its stock and $50,000 in cash to the stockholders of corporation A in exchange for their stock in corporation A. Under the existing law, the $50,000 distributed with the stock of corporation B would be taxed, not as a dividend, but as a capital gain, subject only to the 12½ per cent rate. The effect of such a distribution is obviously the same as if the corporation had declared out as a dividend its $50,000 earnings and profits. If dividends are to be subject to the full surtax rates, then such an amount so distributed should also be subject to the surtax rates and not to the 12½ per cent rate on capital gain. * * * [H. Rept. No. 179, 68th Cong., 1st Sess., p. 14. See also S. Rept. No. 398, 68th Cong., 1st Sess., p. 15.]

than stock dividends during the two years of its operation as a successful corporation. In the beginning of 1948 the earned surplus account had a credit balance of $98,800.52 and on September 30, 1948, after the stock had been liquidated, the credit balance was $61,335.99. While there was a business purpose in the liquidation of the minority stockholder's interest, there is doubt in our minds that the old corporation was liquidated for a business purpose other than tax savings. Cf. **Estate of John B. Lewis**, 10 T. C. 1080, affd. 176 F. 2d 646. No one can ignore the fact that the substance of the old corporation's business was carried on by the new corporation; in fact initially the business was carried on in the same building. In addition, control of both corporations was vested in the same two stockholders. It is our conclusion that the distribution was made pursuant to a plan of reorganization and that the distribution was in effect a taxable dividend. Therefore, it should be taxed to each distributee under section 112 (c) (2). The respondent must be sustained.

Perhaps a word about petitioner's contentions would be proper. Petitioner maintains that the gains he received were the result of a transaction within the contemplation of section 115 (c)[2]. This section provides that amounts distributed in complete liquidation of the corporation shall be treated as a full payment in exchange for the stock.

Under petitioner's contentions the facts would have to support a finding that there was only a liquidation of the old corporation rather than a reorganization. Under this

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[2] *Sec. 115. Distributions by Corporations.*

* * * * * * *

(c) Distribution in Liquidation.—Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112. * * *

argument, where there were a series of transactions whereby the stockholders of the old corporation became stockholders in the new, each transaction must be considered as separate and distinct. Under this theory we must consider that petitioner sold his stock to the old corporation, and we must ignore all other transactions.

The record before us could not support this finding. Take for instance the time relationship between some of these transactions. On April 26, 1948, at a special meeting of the stockholders of the old corporation, petitioner advised them that Davis wished to resign. There followed a discussion after which it was decided to liquidate the old corporation at the earliest date. Four days later, on May 1, Liddon Pontiac, Inc., was incorporated and on the same day the new corporation, with petitioner as the principal party, received a franchise for the sale of Pontiac automobiles. During the next four months the old corporation was completely liquidated and the new continued its business. The synchronization of these transactions is something more than mere coincidence. It appears to us as a plan of reorganization. And since the liquidation was part of the plan, respondent must be sustained.

Reviewed by the Court.

Decisions will be entered under Rule 50. Raum, Bruce, Fisher and Baar, JJ., concur in the result.

APPENDIX B.

PROCEEDINGS IN THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT.

Causes Argued and Submitted.

October 20, 1955—Before: Simons, Chief Judge, McAllister and Stewart, Circuit Judges.

These causes are argued by John J. Hooker for petitioners and by I. Henry Kutz for respondent and are submitted to the court.

Judgment.

Case No. 12,397.

(Filed February 11, 1956.)

On Petition to Review a decision of the Tax Court of the United States.

This cause came on to be heard on the transcript of record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the decision of the said Tax Court in this cause be and the same is hereby reversed and the case remanded to the Tax Court for further proceedings consistent with the opinion herein.

Judgment.

Case No. 12,398.

(Filed February 11, 1956.)

On Petition to Review a decision of the Tax Court of the United States.

This cause came on to be heard on the transcript of record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this court that the decision of the said Tax Court in this cause be and the same is hereby reversed and the case remanded to the Tax Court for further proceedings consistent with the opinion herein.

Opinion.

(Filed February 11, 1956.)

Nos. 12397 and 12398.

UNITED STATES COURT OF APPEALS
For the Sixth Circuit.

William Liddon, Petitioner, 12397 v. Commissioner of Internal Revenue, Respondent.	On Petitions to review the decisions of the Tax Court of the United States.
Maria Prothro Liddon, Petitioner, 12398 v. Commissioner of Internal Revenue, Respondent.	

Decided February 11, 1956.

Before Simons, Chief Judge, McAllister and Stewart, Circuit Judges.

Stewart, Circuit Judge. The sole issue to be determined on this review is whether amounts distributed to the peti-

tioners in 1948 by a closely held corporation were taxable as ordinary income or as a long term capital gain. The Tax Court found that the amounts in question were distributed as "boot" pursuant to a plan of reorganization, having "the effect of the distribution of a taxable dividend" under section 112 (c) (2) of the Internal Revenue Code of 1939. The petitioners contend the distribution was made in complete liquidation of the corporation and that it should therefore be taxed as a long term capital gain under section 115 (c) of the 1939 Code. The facts are not in dispute.

The petitioners were husband and wife in 1948. Together they owned eighty per cent of Liddon Motors, Inc., a Tennessee corporation, hereinafter called the "old corporation," engaged in the business of selling and servicing automobiles under a franchise dealer contract with the Pontiac Motor Division of the General Motors Corporation, hereinafter called "Pontiac." The petitioner husband was president and the petitioner wife was vice president of the corporation. The remaining twenty per cent of the stock was owned by R. H. Davis, the general manager of the corporation.

Among other things the franchise agreement provided: "Third: This Agreement constitutes a personal contract, having been entered into in reliance upon and recognition of W. M. Liddon, R. H. Davis (jointly), the Dealer, or partner(s) in the dealership, or representative(s) of the Dealer who actively and substantially participate(s) in the ownership and/or operation of the dealership. Dealer shall not transfer nor assign this Agreement or any part thereof, nor make nor suffer to be made any substantial change in the ownership, financial interests or active management of Dealer." It was elsewhere provided in the contract that Pontiac could terminate the agreement immediately upon the "Death, incapacity, or the removal, resig-

nation, withdrawal, or elimination from the dealership . . . of . . . any person named in Paragraph Third of this Agreement."

In April of 1948, because of ill health, Davis tendered his resignation as general manager of the corporation, and also notified the petitioners that he wished to sell or liquidate his interest in the corporation as soon as possible. On April 27, 1948, Davis wrote to Pontiac, advising that he had tendered his resignation, that he was "liquidating my stock ownership" and that it was "agreeable with me that in any future contracts between Pontiac Motor Division and Liddon Motors, Inc., or their successors, that I not be considered in Paragraph 3 of the contract."

Special meetings of the stockholders and of the directors of the old corporation were held on April 26, 1948. The minutes of those meetings recite that Davis offered his stock for sale to the other stockholders (petitioners) at book value, but that they did not accept. The minutes further recite that it was after further discussion "concluded by all stockholders that the practical and equitable way to liquidate the stock as requested by Mr. Davis would be to surrender the Charter of the Corporation, selling the assets of the Corporation and liquidating the Corporation at the earliest possible date." Accordingly, the corporation officers were authorized and directed to proceed to liquidate the corporation and surrender its charter, "and sell the assets of the corporation, calling the outstanding stock, and distributing the proceeds to the stockholders in their rightful proportion and share."

On May 1, 1948, Liddon Pontiac, Inc., hereinafter called the "new corporation" was incorporated by the petitioners under the laws of Tennessee. Its initial capital consisted of $5,000 contributed by the petitioners in cash, in addition to a $10.00 qualifying share held by a third party. Within three weeks the petitioners contributed an additional $20,-

000 to the capital of the new corporation. This total contribution of $25,000 was made from the petitioners' personal funds.

On the day of its creation the new corporation entered into a franchise dealer agreement with Pontiac. This new agreement was essentially the same as the previous agreement between Pontiac and the old corporation, except that only the name of W. M. Liddon was entered in "Paragraph Third" of the new agreement, instead of the names of both Liddon and Davis. Pontiac had cancelled the old agreement some time between April 27, the date of Davis' letter, and May 1, the date of the agreement with the new corporation.

On May 6, 1948, at a special meeting of its Board of Directors, the old corporation was directed to sell its operating assets to the new corporation at book value, to permit the new corporation to use the remaining physical assets without charge pending negotiation for their sale, and to transfer its employees' retirement fund to the new corporation. The new corporation accepted this arrangement.

At another special meeting of its Board of Directors, held on July 4, 1948, the old corporation was authorized to pay Davis $11.00 per share for his stock, its approximate book value. On the same day, the old corporation gave Davis its check for $22,000 and his shares were retired. At a subsequent meeting on July 13, 1948, the old corporation was authorized to distribute the balance of its assets to its two remaining stockholders, the petitioners. These assets, consisting of more than $150,000 in cash and notes, were promptly paid over to petitioners in equal shares. Four days later the old corporation surrendered its charter. Each petitioner reported the amount received, less the cost of his old corporation stock, as long term capital gain for 1948.

The Commissioner asserted a deficiency, claiming that these amounts should have been reported by the petitioners as ordinary income. In a decision reviewed by the full court the Tax Court sustained the Commissioner. 22 T. C. 1220.

Considering the above-described series of transactions as a whole, the Tax Court concluded that they evidenced a plan of reorganization. "The synchronization of these transactions is something more than mere coincidence. It appears to us as a plan of reorganization. And since the liquidation was part of the plan, respondent must be sustained." 22 T. C., at 1228.

Since the old corporation had transferred part of its assets to the new corporation, and since immediately after the transfer the old corporation's shareholders were in control of the new corporation, the court pointed out that the transaction fell precisely within one of the statutory definitions of a reorganization.[1]

Moreover, since at the beginning of the series of transactions the petitioners held stock in the old corporation, and at the end they held stock in the new corporation, plus "money-to-boot," the court reasoned that, although there was not a direct exchange of stock in the old corporation for stock in the new, plus "other property or money," that was the net effect of what was done. Accordingly, the court concluded that the case was governed by sections 112 (b) (3) and 112 (c) of the 1939 Code.

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[1] Section 112 (g) (1) provided in part: "The term 'reorganization' means . . . (D) a transfer by a corporation of all or a part of the assets to another corporation if immediately after the transfer the transferor or its shareholders or both are in control of the corporation to which the assets are transferred. . . ." Subsection 112 (h) provided: "As used in this section the term 'control' means the ownership of stock possessing at least 80 per centum of the total combined voting power of all classes of stock entitled to vote and at least 80 per centum of the total number of shares of all other classes of stock of the corporation."

If those sections of the Code control, the result reached by the court was obviously correct, as petitioners in effect concede. Under section 112 (b) (3) no gain was recognizable on the "exchange" of stock in the old corporation for stock in the new.[2] The gain resulting from the distribution of the "other property or money," however, since it did not exceed the value of such "other property or money" was recognizable in full by virtue of section 112 (c) (1),[3] and since the recognizable gain did not exceed the undistributed earnings and profits of the old corporation, it could properly be taxed as a dividend under section 112 (c) (2).[4] **Commissioner v. Estate of Bedford**, 325 U. S. 283 (1945).

The Tax Court not only relied upon the fact that one of the statutory definitions of a reorganization had been formally met, but also emphasized the substance of the situation presented, i. e., when the series of transactions

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[2] Section 112 (b) (3) of the Internal Revenue Code of 1939 provided: "No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization."

[3] Section 112 (c) (1) provided: "If an exchange would be within the provisions of subsection (b) . . . (3) . . . of this section if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph . . . to be received without the recognition of gain, but also of other property or money, then the gain, if any, to the recipient shall be recognized, but in an amount not in excess of the sum of such money and the fair market value of such other property."

[4] Section 112 (c) (2) provided: "If a distribution made in pursuance of a plan of reorganization is within the provisions of paragraph (1) of this subsection, but has the effect of the distribution of a taxable dividend, then there shall be taxed as a dividend to each distributee such an amount of the gain recognized under paragraph (1) as is not in excess of his ratable share of the undistributed earnings and profits of the corporation accumulated after February 28, 1913. The remainder, if any, of the gain recognized under paragraph (1) shall be taxed as a gain from the exchange of property."

was completed the petitioners were in control of the same going business as before, albeit in a new corporate shell, having in the meantime extracted a substantial portion of the accumulated earnings and profits of the business.

In asking us to reverse the Tax Court's decision the petitioners place prime reliance upon the decision of this court in **United States v. Arcade Co.**, 203 F. (2d) 230 (6 Cir., 1953). The facts in that case were significantly different, however, as Judge McAllister's opinion in that case makes clear. There, the old corporation was dissolved and its assets distributed to trustees for its stockholders. Thereafter, at the direction of the stockholders, the trustees transferred the assets to a newly formed corporation in return for its stock, which the trustees delivered to the stockholders in shares proportionate to their ownership in the former corporation.

The opinion in the **Arcade Co.** case emphasizes that the circumstances did not fall within any statutory definition of a reorganization. "It is our conclusion that there was no transfer by the old corporation of its assets to the new corporation, within the meaning of section 112 (g) (1); that neither the old nor the new corporation was a 'party to a reorganization', as set forth in section 112 (g) (2); and that the transactions out of which this controversy arose did not constitute a reorganization within the intendment of the Internal Revenue Code." 203 F. (2d) at 235. The case of **Braicks v. Henricksen**, 43 F. Supp. 254 (D. C. Wash., 1942), aff'd 137 F. (2d) 632 (9 Cir., 1943), also relied upon by petitioners, involved facts almost identical to those in the **Arcade Co.** case. In the present case, on the other hand, the statutory definition of a reorganization was precisely met. The old corporation's assets were transferred directly to the new corporation, and the petitioners were controlling stockholders of both. Therefore,

quite unlike the situation in the **Arcade Co.** case, each corporation was a "party to a reorganization."[5]

The petitioners contend, however, that where a corporation has been liquidated, as the old corporation in the present case clearly was, the provisions of section 115 (c) of the Code relating to the effect of liquidation distributions must prevail over the previously cited sections relating to reorganizations.[6] It is argued that this court has decided that where there has been a liquidation there can be no reorganization. The argument is based on a statement in the opinion in **Mascot Stove Co. v. Commissioner**, 120 F. (2d) 153, at 156 (6 Cir., 1941)—". . . liquidation is the antithesis of reorganization." What the court was there referring to was liquidation in bankruptcy, as the first part of the sentence from which the quotation was lifted clearly indicates. "In the present case the bankruptcy proceeded to liquidation and liquidation is the antithesis of reorganization." Even a casual reading of the balance of Judge Simons' opinion in that case reveals that what the court there decided was that, since the old corporation was adjudicated a bankrupt, its shareholders had nothing to transfer. "The insolvency of the old company, its adjudication as a bankrupt, and the sale of all of its assets for less than its debts, put a period to its existence. The new company was a separate enterprise and its realized gains are taxable." 120 F. (2d), at 156.

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[5] Section 112 (g) (2) of the Internal Revenue Code of 1939 provided that: "The term 'a party to a reorganization' includes a corporation resulting from a reorganization and includes both corporations in the case of a reorganization resulting from the acquisition by one corporation of stock or properties of another."

[6] Section 115 (c) of the Internal Revenue Code of 1939 provided a pertinent part: "Amounts distributed in complete liquidation of a corporation shall be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation of a corporation shall be treated as in part or full payment in exchange for the stock. The gain or loss to the distributee resulting from such exchange shall be determined under section 111, but shall be recognized only to the extent provided in section 112."

That liquidation of a corporation may be and often is one of the steps in a plan of reorganization has, on the other hand, frequently been recognized by this and other courts. "Since the exchange was pursuant to a plan of reorganization, the fact that the Fisher Body Corporation was completely liquidated is not controlling." **Fisher v. Commissioner,** 108 F. (2d) 707, 709 (6 Cir., 1939). "The so-called liquidating dividend was but a step, albeit an essential one, in the reorganization." **Love v. Commissioner,** 113 F. (2d) 236, 238 (3 Cir., 1940). "The liquidation of the old company does not change matters because a statutory reorganization may encompass as one of its incidents the liquidation of one of the corporations a party to the reorganization." **Lewis v. Commissioner,** 176 F. (2d) 646, 649 (1 Cir., 1949).

The petitioners' further argument that because Davis' share in the business was completely liquidated during the progress of the transactions, there could be no reorganization within the intendment of the statute, is lacking in merit. It is not unusual in the process of corporate reorganizations for minority shareholders to liquidate their interests and withdraw. "It is our conclusion that the transaction in controversy amounted to a reorganization . . .; and it is unimportant that, in the transaction, a small number consented, or raised no objection to their elimination as stockholders" (citing cases). **Sieberling Rubber Co. v. Commissioner,** 169 F. (2d) 595, 598 (6 Cir., 1948): "We attach no importance to the fact that some of the stockholders in the transferring corporation acquired no interest in the transferee." **Miller v. Commissioner,** 84 F. (2d) 415, 418 (6 Cir., 1936).

Moreover, we are of the opinion that the Tax Court was correct in analyzing what was done in this case from the point of view of its overall net effect, rather than to permit one isolated transaction in a series to determine

the tax consequences. The tax law, as has been often said, seeks generally to deal with substance rather than form, and particularly is this so in reorganization cases. "Transitory phases of an arrangement frequently are disregarded under these sections of the revenue acts where they add nothing of substance to the completed affair. . . . Here they were no more than intermediate procedural devices utilized to enable the new corporation to acquire all the assets of the old one pursuant to a single reorganization plan." **Helvering v. Alabama Asphaltic Limestone Co.**, 315 U. S. 179, 184-185 (1942). See **Sieberling Rubber Co. v. Commissioner,** supra, 169 F. (2d) at 599; **Miller v. Commissioner,** 103 F. (2d) 58, 59 (6 Cir., 1939); **Lewis v Commissioner,** supra, **Love v. Commissioner,** supra.

For the reasons expressed we think there was no error in the Tax Court's conclusions, with one important exception. The exception to which we refer is the failure of the Tax Court to give any consideration to the $25,000 contribution which petitioners made from their personal funds to the new corporation prior to the distribution to them of the liquid assets of the old. While it was proper for the Tax Court to determine the tax consequences upon the basis of the unitary effect of all that was done, it was not proper to disregard a significant component part in analyzing the whole.

To the extent of this $25,000 the amount distributed did not have "the effect of the distribution of a taxable dividend;" its effect was the repayment of an advance. Moreover, considering the series of transactions as a whole, the net effect of the $25,000 advance made to the new corporate shell in which the business was to be conducted, prior to the distribution made from the old corporate shell in which the business had been conducted, was pro tanto, to reduce the amount of that distribution.

The $25,000 stayed in the going business, just as though it had been transferred directly from the old to the new corporation, and as to it no gain was properly recognizable.

For the reasons expressed, the decisions of the Tax Court are reversed and the cases are remanded for further proceedings consistent with this opinion.

McAllister, Circuit Judge, dissenting. I am of the opinion that the transaction whereby the new corporation acquired the assets of the old company was not a reorganization under Section 112(g) of the Internal Revenue Code, Title 26 U. S. C. A., Section 112(g).

The old corporation, Liddon Motors, Inc., because of the retirement of General Manager Davis, lost its most important business asset—its franchise dealer contract with the Pontiac Division of General Motors Corporation. There was nothing false, suspicious, or contrived about this situation. The company had originally, in 1936, commenced business as a corporation with William Liddon, Maria Liddon, his wife, and R. H. Davis as the stockholders. Some time later, the business was changed to a partnership with the three stockholders carrying on as partners. Then, in 1946, upon the return of Mr. Liddon from service with the armed forces, the partnership was changed to a corporation with the three partners as stockholders.

The company had started in 1936 with a franchise dealer contract with Pontiac Division of General Motors Corporation. Whenever there was a change from the corporate form to a partnership and then back to a corporation, the officers or partners of the company would be obliged to apply to General Motors for consent to an assignment of the franchise to the succeeding organization, even though the partners were the same persons as the stockholders in the corporation. Moreover, each year, General Motors would call for the surrender of the dealer's contract and issue a new one.

The dealer's franchise contract with General Motors provided:

> ". . . this agreement constitutes a personal contract having been entered into in reliance upon and recognition of W. M. Liddon, R. H. Davis, jointly, the dealer or partners in the dealership or representatives of the dealer who actively and substantially participate in the ownership and/or operation of the dealership, dealer shall not transfer nor assign this agreement or any part thereof nor make nor suffer to be made any substantial change in the ownership, financial interest, or active management of the dealer."

R. H. Davis was General Manager of the corporation. He was the man upon whom General Motors relied during the four years' absence of Mr. Liddon while on service with the Army.

The dealer's franchise agreement provided:

> "[General Motors Corporation] may terminate this agreement immediately by delivering to dealer or his representative written notice of such termination in the event of the happening of any of the following:
>
> "(a) Death, incapacity or the removal, elimination or resignation from the dealership for any reason of the dealer or any person named in paragraph third of this agreement."

In April of 1948, Mr. Davis had a heart attack. On the urgent advice of his physicians, he was obliged to give up all business connections. On April 26, 1948, he tendered his resignation as General Manager of the company by letters addressed to Mr. Liddon, the President, and to the Pontiac Division of General Motors. Upon receipt of the notice of his resignation, General Motors, in accordance with the contract provisions, immediately cancelled the dealer's franchise contract.

The Liddon Company, on April 26, 1948, the day of Mr. Davis' resignation, held a meeting of the Board of Directors for the purpose of liquidating the company and surrendering its charter. At that time, Mr. Davis offered his stock for sale, but a price could not be agreed upon.

On May 1, 1948, after the liquidation of the old corporation had been determined upon and while it was under way, but before it became completely consummated, a new corporation, Liddon Motors, Inc., was formed, in which William Liddon owned 1,250 shares, Maria Liddon, his wife, owned 1,250 shares, and Oscar Sanders owned one share. This new corporation was formed with $3,000 in cash from Mr. Liddon, $2,000 in cash from Mrs. Liddon, and $10 from Mr. Sanders. It was immediately chartered and undertook to commence business. It had received no assets of any kind from the old company then in process of liquidation. When the new corporation was formed on May 1, 1948, General Motors Corporation issued a dealer's franchise contract to William Liddon, the sole designated individual in the agreement. Later on, May 21, 1948, Mr. and Mrs. Liddon contributed an additional $20,000 of their own money to the new corporation. At that time, none of the assets of the old company had been received by the new company or by Mr. and Mrs. Liddon through sale, transfer, or otherwise. All of the capital in the new corporation—aggregating more than $25,000—was new and had no connection or relationship, directly or indirectly, with the old company.

Prior to the contribution of the last $20,000 to the new corporation by Mr. and Mrs. Liddon, the Board of Directors of the old corporation directed sale of its operating assets to the new corporation at book value, and agreed to permit the new corporation to use the remaining physical assets without charge, pending negotiation for their sale, as well as directing the transfer of its employees' retirement fund to the new corporation.

The government emphasizes the above directions of the old corporation as to the sale of its assets and the transfer of the employees' retirement fund, but I fail to perceive how this affects the case. The old corporation certainly was able to receive more for its assets from the new corporation than it could from anyone else, as a considerable amount of it was concerned with such a dealership; and the transfer of the employees' retirement fund might result in some security for the old employees and be an inducement to them to work for the new company, but beyond that consideration, I fail to see that this is a factor to be considered in arriving at the conclusion that the transaction amounted to a reorganization within the meaning of the statute.

The new corporation, on June 4, 1948, purchased a quantity of the assets of the old company. It was an outright sale. Mr. Davis never recovered his health and never resumed any business association. The old corporation finally paid him $11 per share for his stock, which was the same value it would have had upon final liquidation. It also paid off its bills and liquidated its accounts receivable during the first three months that the new corporation was operated, and, finally, it was completely liquidated.

It appears to me that the Commissioner has failed to establish that there was a reorganization within the intendment of the statute.

The new corporation was an entirely different entity. The stockholders were different, although the difference in shares between the stockholders in the old corporation and in the new company would not, in itself, prevent the transaction from being found to be a reorganization. But the new company was formed with new money. It had a new dealer's franchise contract. It bought out the assets of the old corporation, paying cash to that company.

There was no way in which the old company could transfer its most important asset to the new company, since the dealer's franchise contract depended entirely upon the action of General Motors Corporation; and, according to its terms, the franchise of the old company had come to an end with the retirement of Mr. Davis. The testimony in the record shows that the new franchise was issued by General Motors because Mr. Liddon, as an individual, was able to fulfill the financial and other requirements exacted. There was no way that he could have secured such a contract except by complying with the requirements prescribed by General Motors and justifying the faith that that company had in his personal ability and integrity. It might be said that General Motors would have, in any event, awarded the dealership to Mr. Liddon, if he desired it, and qualified for it, and continued to engage in the business of selling cars. That may be so. But the choice was theirs, and not his; and it was a valuable asset, and they might have, as has happened in similar situations, awarded it to someone else. When General Motors issued the new and different dealer's franchise contract, it was an asset that could not have been secured from the old company on any terms.

If General Motors had refused the new corporation the dealer's franchise contract, or if the new corporation had secured a dealer's franchise contract from a company other than General Motors, it is admitted that the claim that the new company was merely a reorganized corporation could not be maintained. I am unable to see any difference in the situation where the contract with the old company had been cancelled and the sole power to grant such a contract to the new company lay entirely in the discretion of General Motors Corporation. For that seems clearly to disclose that the new company was not a mere continuation of the old one; and the fact that the new company bought the assets of the old company with new capital does not,

in my view, lead to the conclusion that the transaction was only a transfer of property from the one corporation to a newly organized company, which, in effect, was the same. In my opinion, the decision of the Tax Court should be reversed.

Nos. 12,397, 12,398.

In the
UNITED STATES COURT OF APPEALS
For the Sixth Circuit.

No. 12,397.

William Liddon

v.

Commissioner of Internal Revenue.

No. 12,398.

Maria Prothro Liddon

v.

Commissioner of Internal Revenue.

Petition to Rehear.

John J. Hooker,
K. Harlan Dodson, Jr.,
1106 Nashville Trust Building,
Nashville 3, Tennessee,
Attorneys for Petitioners.

(Filed Feb. 27, 1956. Carl W. Reuss, Clerk.)

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Come now the petitioners and respectfully pray this Honorable Court to grant them a rehearing in these causes and move the Court that the opinion handed down by this Court on February 11, 1956, and the judgment rendered thereon be vacated and that judgment be rendered in this Court reversing the Tax Court upon the following grounds:

I.

The transfer of assets from Liddon Motors, Inc. (referred to in the opinion of this Court as the "old corporation"), to Liddon Pontiac, Inc. (referred to by this Court in its opinion as the "new corporation"), was not a transfer within the meaning of Section 112 (g) (1) of the Internal Revenue Code but was a bona fide sale for cash and therefore falls within the distinction noted by this Honorable Court in the case of **Glenn v. Courier-Journal Job Printing Company**, 127 F. (2d) 820.

II.

The distinction noted by this Court between these cases and the cases of **United States v. Arcade Company**, 203 F. (2d) 230, and **Braicks v. Henricksen**, 43 F. Supp. 254, is that in the latter cases the conduit of property formerly belonging to the old corporation, which eventually found its way into the hands of the new corporation, was through trustees; whereas, in the cases at bar there was an outright sale of some assets from the old corporation to the new corporation, which proceeds of sale, together with the balance of the other net assets of the old corporation, were distributed to the stockholders of the old corporation in **complete** liquidation. Such difference or distinction is a distinction of form only and not one of substance and therefore under the rule enunciated by this Court in these cases is not a distinction or difference to be considered.

III.

While it is true that the quotation "liquidation is the antithesis of reorganization" is taken from the opinion of this Court in the case of **Mascot Stove Company v. Commissioner**, 120 F. (2d) 153, which case is obviously distinguishable from the cases at bar, this Court in the case of **Glenn v. Courier-Journal Job Printing Company**, 127 F. (2d) 820, adopted this same quotation in a case involving Section 112 (g) of the Internal Revenue Code in finding that there was no reorganization within the intention of Section 112 (g).

A Bona Fide Sale of Assets Is Not Within the Concept "Transfer" of Section 112 (g).

The Tax Court and the various District Courts have frequently recognized that where there is an outright sale of assets the result sought to be reached in Section 112 of

the Internal Revenue Code of 1939 is not involved. For example, the Supreme Court of the United States in the cases of **Helvering v. Minn. Tea,** 296 U. S. 378, 56 S. Ct. 269, 80 L. Ed. 284, and **Pinellas Ice and Coal Storage Company v. Commissioner,** 287 U. S. 462, 53 S. Ct. 257, 77 L. Ed. 428, held that the sale of a company's assets for cash does not constitute a reorganization. While these cases were exchange cases under other portions of Section 112, they indicate the Court's conclusion that sales for cash are to be distinguished from other transfers under the theory of Section 112 and have been often cited for that legal proposition, for example, **Commissioner v. Kitselman** (Seventh Circuit), 89 F. (2d) 458, and **Cortland Specialty Company v. Commissioner** (Second Circuit), 60 F. (2d) 937.

In this Court's opinion in the case of **Glenn v. Courier-Journal Job Printing Company,** supra, there was a transfer of assets at a fair price, and this Court found that "there was no continuity of interest **resulting from the transfer of the assets.**" While the factual situation in the **Courier-Journal** case is obviously distinguishable from the factual situation in the cases at bar, the basis upon which the **Courier-Journal** case was determined is actually analogous to the cases at bar.

This Case Is Distinguishable From the Arcade Company and the Braicks v. Henricksen Cases Only as to Form and Not as to Substance.

This Court, the Supreme Court of the United States, the various Circuit Courts and District Courts, as well as The Tax Court, have held in so many cases that **substance** and not **form** is controlling in tax cases that the citation of authority would be trite. Indeed, that is the premise upon which The Tax Court and this Court in the majority opinion determined the instant cases. We have no fault to find with this well established premise, but we do respect-

fully but earnestly submit that, after stating such to be the premise, this Court violated that premise in attempting to distinguish away the **Arcade Company** and the **Braicks v. Henricksen** cases. In those cases the old corporation was dissolved, as was the case here. However, in those cases all of the assets were distributed to trustees for the stockholders and then exchanged by the trustees for stock in the newly formed corporation. The only distinction in the cases at bar is that no subterfuge was used, and, on the contrary, there was a bona fide sale for cash of a small part of the assets of the old corporation,* and the only reason these assets were sold to the new corporation rather than to someone else was because the new corporation was the only market in which such peculiar assets could be sold for their reasonable value. If the distinction noted by this Honorable Court be valid, then the result is that this Court has said that if the Liddons had adopted the subterfuge of distributing some of the assets of the old corporation to trustees and let the trustees sell to the new corporation, there would not have been a Section 112 (g) reorganization, but if the subterfuge is not used, there is a Section 112 (g) reorganization. We earnestly submit that this amounts to placing not some, but all, emphasis on **form** and no emphasis on **substance**.

"Liquidation Is the Anthithesis of Reorganization."

The quotation "liquidation is the anthithesis of reorganization" was, as set forth in petitioners' original brief, taken from this Court's opinion in the case of **Mascot Stove Company v. Commissioner**, 120 F. (2d) 153. Petitioners did not mean to insinuate then, nor do they intend

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* The proceeds from the sale of these few assets were distributed along with all of the other assets of the old corporation to its stockholders in complete liquidation and *no part* of these assets received in liquidation went into the new corporation.

to insinuate now, that there is any factual similarity between the **Mascot Stove Company** case and the cases at bar. However, this statement was submitted then, as now, to show that this Court has found in effect that where there is a bona fide liquidation such is not in keeping with a plan of reorganization. This same quotation upon which petitioners relied in their original brief was quoted by this Court from the **Mascot Stove Company** case in the **Glenn v. Courier-Journal Job Printing Company** case (127 F. [2d] 820), where a situation not identical, but similar, to the cases at bar, involving Section 112 (g) of the Internal Revenue Code, was under consideration.

While it is true that the fact that there was a complete liquidation is not controlling in a reorganization case, certainly this Court and other courts have treated the fact that there was a complete liquidation of the old corporation as being an important factor in determining that there was no reorganization.

For all the foregoing reasons we respectfully, we earnestly, pray that this Honorable Court grant this petition for a rehearing in these causes and that the judgment affirming the opinion of The Tax Court be vacated and that the cogent reasoning of the dissenting opinion in these cases be made the opinion of the Court.

Respectfully submitted,

John J. Hooker,
K. Harlan Dodson, Jr.,
1106 Nashville Trust Building,
Nashville 3, Tennessee,
Attorneys for Petitioners.

Certificate of Counsel.

William Liddon and Maria Prothro Liddon, petitioners herein, by their attorney, John J. Hooker, hereby certify that in their judgment and in the judgment of their counsel the foregoing petition for a rehearing is well founded and is not interposed for delay.

John J. Hooker,
Counsel for Petitioners.

Order Denying Rehearing.

(Filed March 9, 1956.)

The petition for rehearing is denied.

Judge McAllister is of the opinion that a rehearing should be granted.